

**DEPARTMENT OF STATE REVENUE**

**LETTER OF FINDINGS NUMBER: 99-0501**

**Use Tax**

**For Tax Years 1996 through 1998**

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**ISSUES**

**I. Use Tax—Steel Floor Grates**

**Authority:** 45 IAC 2.2-5-8

Taxpayer protests imposition of use tax on steel floor grating.

**II. Use Tax—Boiler Vacuum**

**Authority:** 45 IAC 2.2-5-8

Taxpayer protests imposition of use tax on a boiler vacuum.

**III. Use Tax—Steel Drain Covers**

**Authority:** 45 IAC 2.2-5-8

Taxpayer protests imposition of use tax on steel grate drain covers.

**IV. Use Tax—Front Loader Tractor**

**Authority:** IC 6-2.5-5-4; 45 IAC 2.2-5-8

Taxpayer protests imposition of use tax on a front loader tractor.

**STATEMENT OF FACTS**

Taxpayer is engaged in the production of flowers. Taxpayer forces the flowers to grow out of season via artificial temperature and humidity control. As a result of an audit for the tax years in

question, the Department issued proposed assessments on several items. Taxpayer protests four of the items assessed use tax. Further facts will be provided as necessary.

**I. Use Tax—Steel Floor Grates**

**DISCUSSION**

Taxpayer uses steam tubes in a trench (steam pit) to regulate heat and humidity in its greenhouse. Taxpayer purchased steel grates to replace the all-wood cover over the trench to allow a forklift to run over the trench without breaking the steam tubes or the wood trench cover. The grates are covered with plywood sheets in order to regulate the release of heat and to facilitate the passage of workers and a forklift over the steam pipes. The Department assessed use tax on the grating. Taxpayer protests that the grating is necessary since it is directly used to produce its flowers. 45 IAC 2.2-5-8(c) states:

The state gross retail tax does not apply to purchases of manufacturing machinery, tools, and equipment to be directly used by the purchaser in the production process provided that such machinery, tools, and equipment are directly used in the production process; i.e., they have an immediate effect on the article being produced. Property has an immediate effect on the article being produced if it is an essential and integral part of an integrated process which produces tangible personal property.

Taxpayer believes that the grates qualify for this exemption. Taxpayer explained that the flowers must have a specific temperature in order to mature properly. 45 IAC 2.2-5-8(g) states, in part:

“Have an immediate effect upon the article being produced”: Machinery, tools, and equipment which are used during the production process and which have an immediate effect upon the article being produced are exempt from tax. Component parts of a unit of machinery or equipment, which unit has an immediate effect on the article being produced, are exempt if such components are an integral part of such manufacturing unit. The fact that particular property may be considered essential to the conduct of the business of manufacturing because its use is required either by law or by practical necessity does not itself mean that the property “has an immediate effect upon the article being produced”. Instead, in addition to being essential for one of the above reasons, the property must also be an integrated part of an integrated process which produces tangible personal property.

Here, the grates allow the forklift and workers to travel over the steam pit without breaking the plywood covers. The grates serve as protection for the steam pipes, which is a practical necessity. The steam pipes provide the heat and humidity control necessary to keep the greenhouse at the proper temperature and humidity levels. The grates do not provide that control, however, and are therefore not an integral part of an integrated process which produces tangible personal property.

## **FINDING**

Taxpayer's protest is denied.

### **II. Use Tax—Boiler Vacuum**

## **DISCUSSION**

Taxpayer protests imposition of use tax on a vacuum system used to clean tubes in a coal-fired boiler. Taxpayer explains that the boiler burns coal to produce steam which is used to heat the greenhouse where the flowers mature. The boiler requires frequent cleaning in order to operate efficiently. Taxpayer explains that if the boiler was not cleaned at least once a week, it would cease functioning completely.

The relevant regulation is 45 IAC 2.2-5-8(h)(1), which states:

Machinery, tools, and equipment used in the normal repair and maintenance of machinery used in the production process which are predominantly used to maintain production machinery are subject to tax.

The cleaning of the boiler tubes is maintenance and therefore 45 IAC 2.2-5-8(h)(1) establishes that the vacuum system is taxable.

## **FINDING**

Taxpayer's protest is denied.

### **III. Use Tax—Steel Drain Covers**

Taxpayer protests imposition of use tax on steel drain covers it purchased. Taxpayer explains that it switched from hand loading of the flowers in the various growing phases to using a forklift. The forklift broke through the original cast iron drain covers and taxpayer had to use steel covers to accommodate the forklift.

The Department refers to 45 IAC 2.2-5-8(c)(4), which offers examples of equipment that is not exempt:

(F) Ceiling lights for general illumination in the plant area.

Here, the drains are for general drainage, which is similar to the example of ceiling lights used for general illumination listed in 45 IAC 2.2-5-8(c)(4)(F). The drains, and therefore drain covers, do not have an immediate effect on the tangible personal property being produced. The drain covers are taxable.

## **FINDING**

Taxpayer's protest is denied.

### **IV. Use Tax—Front Loader Tractor**

Taxpayer protests the imposition of use tax on the purchase of a front loader tractor. Taxpayer uses the tractor to dig up soil from its fields to plant the flowers in, and also to treat the soil for various diseases found in it which are harmful to the flowers taxpayer grows. Taxpayer believes that these functions are essential parts of the production process, and should therefore be tax exempt.

The Department refers to 45 IAC 2.2-5-8(d), which explains in part:

Pre-production and post-production activities. "Direct use in the production process" begins at the point of the first operation or activity constituting part of the integrated production process and ends at the point that the production has altered the item to its completed form, including packaging, if required.

Taxpayer explains that all growers of this type of flower use the same method and that taxpayer does not know of any other way to move the soil. 45 IAC 2.2-5-8(g) states, in part:

"Have an immediate effect upon the article being produced": Machinery, tools, and equipment which are used during the production process and which have an immediate effect upon the article being produced are exempt from tax. Component parts of a unit of machinery or equipment, which unit has an immediate effect on the article being produced, are exempt if such components are an integral part of such manufacturing unit. The fact that particular property may be considered essential to the conduct of the business of manufacturing because its use is required either by law or by practical necessity does not itself mean that the property "has an immediate effect upon the article being produced". Instead, in addition to being essential for one of the above reasons, the property must also be an integrated part of an integrated process which produces tangible personal property.

The tangible personal property in question here is flowers. The tractor is used to move and treat the soil in which the flowers grow. The moving of the growing medium (soil) is not exempt, as described in 45 IAC 2.2-5-8(g).

However, the tractor also is used to perform the separate function of treating the soil for disease prior to use in the production of flowers. IC 6-2.5-5-4 explains:

Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for his direct use in the direct production of the machinery, tools, or equipment described in section 2 or 3 of this chapter.

Treating the soil for disease is direct use in the direct production of the growing medium used in the production of the flowers, and is therefore exempt as described in IC 6-2.5-5-4.

The fact that these activities are required by practical necessity does not automatically mean that the tractor used to perform them is exempt, as provided by 45 IAC 2.2-5-8(g). The function of moving the soil occurs prior to the production of the flowers, and is properly taxable under 45 IAC 2.2-5-8(d). The function of producing the growing medium (the disease-free soil) is exempt under IC 6-2.5-5-4. Therefore, the tractor is properly subject to use tax to the extent it is used to move soil, and exempt to the extent it is used to treat soil for disease.

### **FINDING**

Taxpayer's protest is sustained in part and denied in part.

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